

**Introduced by Senators Alquist and Maldonado**

(Coauthors: Assembly Members Gordon, Houston, Huff, and Walters)

February 18, 2005

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An act to add Section 6377 to the Revenue and Taxation Code, relating to taxation, and making an appropriation therefor, to take effect immediately, tax levy.

**LEGISLATIVE COUNSEL'S DIGEST**

SB 552, as introduced, Alquist. Sales and use taxes: exemption: telecommunication activities.

The Sales and Use Tax Law imposes a tax on the gross receipts from the sale in this state of, or the storage, use, or other consumption in this state of, tangible personal property, and provides various exemptions from the taxes imposed by that law.

This bill would exempt from those taxes the gross receipts from the sale of, and the storage, use, or other consumption of, tangible personal property, as defined, purchased for use by a qualified person, as defined, in manufacturing, processing, or fabricating of property, or for use in research and development activities and introduced into the process, as specified. This bill would also provide that, for purchases made in calendar years beginning on or after January 1, 2006, the exemption be implemented through a refund procedure commencing on January 1 of the first fiscal year in which the state budget deficit is eliminated, and would continuously appropriate moneys from the General Fund to the State Board of Equalization for the payment of those refunds.

This bill would specify that this exemption would apply to local sales or transactions and use taxes, unless the governing body of the taxing county, city, or district votes otherwise.

Counties and cities are authorized to impose local sales and use taxes in conformity with state sales and use taxes. Exemptions from state sales and use taxes enacted by the Legislature are incorporated into the local taxes.

Section 2230 of the Revenue and Taxation Code provides that the state will reimburse counties and cities for revenue losses caused by the enactment of sales and use tax exemptions.

This bill would provide that, notwithstanding Section 2230 of the Revenue and Taxation Code, no appropriation is made and the state shall not reimburse local agencies for sales and use tax revenues lost by them pursuant to this bill.

This bill would take effect immediately as a tax levy.

Vote:  $\frac{2}{3}$ . Appropriation: yes. Fiscal committee: yes. State-mandated local program: yes.

*The people of the State of California do enact as follows:*

1 SECTION 1. Section 6377 is added to the Revenue and  
2 Taxation Code, to read:

3 6377. (a) For calendar years beginning on or after January 1,  
4 2006, there are exempted from the taxes imposed by this part the  
5 gross receipts from the sale of, and the storage, use, or other  
6 consumption in this state of, by a qualified person any of the  
7 following:

8 (1) Tangible personal property that will become an ingredient  
9 or component part of tangible personal property manufactured,  
10 processed, fabricated or used in research and development  
11 activities.

12 (2) Tangible personal property directly used or consumed in or  
13 during the actual manufacturing, processing, fabrication or  
14 research and development of tangible personal property if the use  
15 or consumption of the property is necessary or essential to the  
16 manufacturing, processing, fabrication operation or research and  
17 development, and directly makes or causes a chemical or  
18 physical change to either of the following:

19 (A) The product being manufactured, processed, fabricated, or  
20 used in a research and development activity.

21 (B) Any intermediate or preliminary product that will become  
22 an ingredient or component part of the product being

1 manufactured, processed, fabricated, or used in a research and  
2 development activity.

3 (3) Actuators, steam production equipment and its fuel,  
4 in-process flow through tanks, cooling towers, generators, heat  
5 exchangers, transformers and the switches, breakers, capacitor  
6 banks, regulators, relays, reclosers, fuses, interruptors, reactors,  
7 arrestors, resistors, insulators, instrument transformers, and  
8 telemetry units that are related to the transformers, electronic  
9 control room equipment, computerized control units, pumps,  
10 compressors, and hydraulic units that are used to power, supply  
11 support, or control equipment that qualifies for exemption under  
12 paragraph (2) or paragraph (6) of this subdivision, or to generate  
13 electricity, chilled water, or steam for ultimate sale.

14 (4) Transformers located at an electric generating facility that  
15 increase the voltage of electricity generated for ultimate sale, the  
16 electrical cable that carries the electricity from the electric  
17 generating equipment to the step-up transformers, and the  
18 switches, breakers, capacitor banks, regulators, relays, reclosers,  
19 fuses, interruptors, reactors, arrestors, resistors, insulators,  
20 instrument transformers, and telemetry units that are related to  
21 the step-up transformers.

22 (5) Transformers that decrease the voltage of electricity  
23 generated for ultimate sale and the switches, breakers, capacitor  
24 banks, regulators, relays, reclosers, fuses, interruptors, reactors,  
25 arrestors, resistors, insulators, instrument transformers, and  
26 telemetry units that are related to the step-down transformers.

27 (6) Tangible personal property used or consumed in  
28 manufacturing, processing, fabrication, or research and  
29 development of tangible personal property if the use or  
30 consumption of the property is necessary and essential to a  
31 pollution control process.

32 (7) Lubricants, chemicals, chemical compounds, gases, or  
33 liquids that are used or consumed during manufacturing,  
34 processing, fabrication, or research and development, of tangible  
35 personal property if their use or consumption is necessary and  
36 essential to prevent the decline, failure, lapse, or deterioration of  
37 equipment exempted by this section.

38 (8) Gases used on the premises of a manufacturing plant or  
39 facility used in performing research and development activities to  
40 prevent contamination of raw material or product, or to prevent a

1 fire, explosion, or other hazardous or environmentally damaging  
2 situation at any stage in the manufacturing or research and  
3 development process, or in loading or storage of the product or  
4 raw material on the premises.

5 (9) Tangible personal property used or consumed during  
6 manufacturing, processing, fabrication, or research and  
7 development of tangible personal property if the use or  
8 consumption of the property is necessary and essential to a  
9 quality control process that tests tangible personal property that is  
10 being manufactured, processed, fabricated, or used in performing  
11 research and development activities.

12 (10) Tangible personal property used or consumed in  
13 manufacturing, processing, fabrication, or research and  
14 development of tangible personal property if the use or  
15 consumption of the property is necessary and essential to comply  
16 with federal, state, or local laws, or rules and regulations that  
17 establish requirements related to public health.

18 (11) Tangible personal property specifically installed to do any  
19 of the following:

20 (A) Reduce water use and wastewater flow volumes from the  
21 manufacturing, processing, fabrication, research and  
22 development or repair operation.

23 (B) Reuse and recycle wastewater streams generated within  
24 the manufacturing, processing, fabrication, research and  
25 development or repair operation.

26 (C) Treat wastewater from another industrial or municipal  
27 source for the purpose of replacing existing freshwater sources in  
28 the manufacturing, processing, fabrication, research and  
29 development or repair operation.

30 (12) Chemicals, catalysts, and other materials that are used  
31 during a manufacturing, processing, fabrication, or research and  
32 development operation to produce or induce a chemical or  
33 physical change, to remove impurities, or to make the product  
34 more marketable.

35 (13) Semiconductor, pharmaceutical or biotechnology  
36 fabrication, or research and development clean rooms and  
37 equipment.

38 (b) For purposes of this section all of the following apply:

1 (1) “Qualified person” means a manufacturer or an entity  
2 performing research and development, or engaged in  
3 telecommunication activities.

4 (2) “Fabricating” means to make, build, create, produce, or  
5 assemble components or property to work in a new or different  
6 manner.

7 (3) “Manufacturing” means the activity of converting or  
8 conditioning property by changing the form, composition,  
9 quality, or character of the property for ultimate sale at retail or  
10 use in the manufacturing of a product to be ultimately sold at  
11 retail. Manufacturing includes any improvements to tangible  
12 personal property that result in a greater service life or greater  
13 functionality than that of the original property.

14 (4) “Process” means the period beginning at the point at which  
15 any raw materials are received by the qualified taxpayer and  
16 introduced into the manufacturing, processing, refining,  
17 fabricating, or recycling activity of the qualified taxpayer and  
18 ending at the point at which the manufacturing, processing,  
19 refining, fabricating, or recycling activity of the qualified  
20 taxpayer has altered tangible personal property to its completed  
21 form if required.

22 (5) “Processing” means the physical application of the  
23 materials and labor necessary to modify or change the  
24 characteristics of property.

25 (6) “Research and development” means those activities that  
26 are described in Section 174 of the Internal Revenue Code or in  
27 any regulations thereunder.

28 (c) For purposes of this section, all of the following apply:

29 (1) The production of a publication for the dissemination of  
30 news of a general character and of a general interest that is  
31 printed on newsprint and distributed to the general public at a  
32 daily, weekly, or other short intervals is considered  
33 manufacturing.

34 (2) The manufacturing or research and development of  
35 computer software begins with the design and writing of the code  
36 or program for the software and includes the testing or  
37 demonstration of the software.

38 (3) “Semiconductor, pharmaceutical or biotechnology  
39 fabrication cleanrooms and equipment” means all tangible  
40 personal property, without regard to whether the property is

1 affixed to or incorporated into realty, used in connection with the  
2 manufacturing, processing, fabrication, or research and  
3 development in a cleanroom environment of a semiconductor,  
4 pharmaceutical, or biotechnology product, without regard to  
5 whether the property is actually contained in the cleanroom  
6 environment. The term includes integrated systems, fixtures, and  
7 piping, all property necessary or adapted to reduce contamination  
8 or to control airflow, temperature, humidity, chemical purity, or  
9 other environmental conditions or manufacturing or research and  
10 development tolerances, and production equipment and  
11 machinery. The term does not include the building or a  
12 permanent, nonremovable component of the building, that houses  
13 the cleanroom environment. The term includes moveable  
14 cleanroom partitions and cleanroom lighting.

15 (d) No exemption shall be allowed under this section unless  
16 the purchaser furnishes the retailer with an exemption certificate,  
17 completed in accordance with any instructions or regulations as  
18 the board may prescribe, and the retailer subsequently furnishes  
19 the board with a copy of the exemption certificate. The  
20 exemption certificate shall contain the sales price of the  
21 machinery or equipment that is exempt pursuant to subdivision  
22 (a).

23 (e) Notwithstanding any provision of the Bradley-Burns  
24 Uniform Local Sales and Use Tax Law (Part 1.5 (commencing  
25 with Section 7200)) or the Transactions and Use Tax Law (Part  
26 1.6 (commencing with Section 7251)), the exemption established  
27 by this section shall apply with respect to any tax levied by a  
28 county, city, or district pursuant to, or in accordance with, either  
29 of those laws, unless the local government that would otherwise  
30 receive the sales tax votes for the exception not to apply.

31 (f) (1) Notwithstanding subdivision (a), the exemption  
32 provided by this section shall not apply to any sale or use of  
33 property which, within one year from the date of purchase, is  
34 either removed from California or converted from an exempt use  
35 under subdivision (a) to some other use not qualifying for the  
36 exemption.

37 (2) Notwithstanding subdivision (a), the exemption established  
38 by this section shall not apply with respect to any tax levied  
39 pursuant to Sections 6051.2 and 6201.2, or pursuant to Section  
40 35 of Article XIII of the California Constitution.

(g) If a purchaser certifies in writing to the seller that the property purchased without payment of the tax will be used in a manner entitling the seller to regard the gross receipts from the sale as exempt from the sales tax, and within one year from the date of purchase, the purchaser (1) removes that property outside California, (2) converts that property for use in a manner not qualifying for the exemption, or (3) uses that property in a manner not qualifying for the exemption, the purchaser shall be liable for payment of sales tax, with applicable interest, as if the purchaser were a retailer making a retail sale of the property at the time the property is so removed, converted, or used, and the sales price of the property to the purchaser shall be deemed the gross receipts from that retail sale.

(h) This section applies to leases of tangible personal property classified as “continuing sales” and “continuing purchases” in accordance with Sections 6006.1 and 6010.1. The exemption established by this section shall apply to the rentals payable pursuant to such a lease, provided the lessee is a qualified person and the property is used in an activity described in subdivision (a). Rentals that meet the foregoing requirements are eligible for the exemption for a period of six years from the date of commencement of the lease. At the close of the six-year period from the date of commencement of the lease, lease receipts are subject to tax without exemption.

(i) (1) The granting of exemptions pursuant to this section for purchases made in calendar years beginning on or after January 1, 2006, shall be postponed until after January 1 of the first fiscal year in which the state budget deficit is eliminated, and shall be granted thereafter in the form of a refund to a qualified person, only upon submission by a qualified person of a claim for refund to, and acceptance of the claim by, the board, as provided in paragraph (2).

(2) A qualified person who has paid sales tax reimbursement to a retailer or use tax on a purchase or purchases of property for which an exemption is allowed pursuant to this section for purchases made in calendar years beginning on or after January 1, 2006, may file a claim for refund equal to the tax on the exempt amount that would otherwise be allowed pursuant to this section. Any claim so filed shall be submitted to the board on a form prescribed by the board, and may be filed no earlier than the

1 date of the transaction for which a sales tax exemption under this  
2 section is allowed. A claim for refund shall, unless the sale or use  
3 of the property is otherwise exempt under this part, be  
4 accompanied by proof of payment of the tax to a retailer,  
5 including, but not limited to, a copy of an invoice or purchase  
6 contract that indicates the following:

7 (A) The date on which the purchase occurred.

8 (B) A description of the property purchased.

9 (C) The price paid for the property.

10 (D) The amount of tax paid with respect to the purchase.

11 (3) In the case of a person who has self-reported use tax to the  
12 board, the claim for refund shall also indicate the amount of use  
13 tax paid and the period for which that tax was remitted.

14 (4) Interest shall be paid on any refund made pursuant to this  
15 section.

16 (5) Notwithstanding Section 6961, the board may recover any  
17 refund or part thereof that is erroneously made pursuant to this  
18 section. In recovering any erroneous refund made pursuant to this  
19 section, the board, in its discretion, may issue a deficiency  
20 determination in accordance with Article 2 (commencing with  
21 Section 6481) of Article 4 (commencing with Section 6536) of  
22 Chapter 5. Except in the case of fraud, that determination shall be  
23 made within three years from the last day of the month following  
24 the quarterly period in which the board approved the refund.

25 (6) Any refund approved by the board pursuant to this section  
26 shall be payable from the General Fund.

27 (7) Notwithstanding Section 13340 of the Government Code,  
28 the amount necessary for the payment of refunds approved under  
29 this subdivision is hereby continuously appropriated, without  
30 reference to fiscal year, from the General Fund to the State Board  
31 of Equalization for the payment of those refunds.

32 SEC. 2. Notwithstanding Section 2230 of the Revenue and  
33 Taxation Code, no appropriation is made by this act and the state  
34 shall not reimburse any local agency for any sales and use tax  
35 revenues lost by it under this act.

36 SEC. 3. This act provides for a tax levy within the meaning of  
37 Article IV of the Constitution and shall go into immediate effect.